



THE COMMONWEALTH OF MASSACHUSETTS  
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SENT ELECTRONICALLY, BY FAX AND MAIL

December 12, 2002

Mary Cottrell, Secretary  
Department of Telecommunications and Energy  
One South Station, 2nd Floor  
Boston, MA 02110

RE: Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company, D.T.E. 02-78

Dear Secretary Cottrell:

On November 27, 2002, the Boston Edison Company, Cambridge Electric Light Company, Commonwealth Electric Company and NSTAR Gas Company ("NSTAR" or Company") filed a request with the Department of Telecommunications and Energy ("Department") for an accounting deferral related to pension and post-retirement benefits other than pensions ("PBOP"). On the same day, the Department issued a Notice of Inquiry that set December 9, 2002, as the deadline for submitting comments on the Company's filing, which has been extended until today. Since the Company has not demonstrated a *prima facie* case entitling it to the deferral, the Department should either deny the petition outright or at least allow discovery and conduct an evidentiary hearing on the petition prior to ruling on the request. *North Attleboro Gas Company*, D.P.U. 93-229, p. 7 (1993).

Generally Accepted Accounting Principles ("GAAP") require the Company to record on its financial statements (1) its expected liabilities associated with its pension plan and PBOP, and (2) the assets associated with their respective trust funds. Pension accruals booked each year vary and are somewhat subjective; they involve actuarial expectations of the returns on the trust funds, the rise in health care costs, the mortality of the employees, and the expected discount rate. All of these assumptions change over time, and therefore, the Company's pension and PBOP liabilities change over time. The annual pension liability changes flow through to the Company's bottom line and affect its reported earnings from year to year. These changes, however, may have little or no effect on the actual cash flow or out-of-pocket costs that the Company will incur in any given year. The Company proposes that the Department, until it may

otherwise order, allow the Company to: (a) defer, and record as a regulatory asset or liability, the difference between the level of the pension and PBOP expenses that are included in rates and the amounts that must be booked in accordance with FAS 87 and FAS 106; and (b) defer as a regulatory asset the amount of its current and future Additional Minimum Liability to reflect the Company's ability to recover in rates over time its actual pension liability.

The Department has a clear standard for reviewing petitions, such as the one NSTAR filed here, for deferral accounting treatment. *North Attleboro Gas Company*, D.P.U. 93-229, p. 7-8 (1994).<sup>1</sup> A company must make a *prima facie* showing in its petition that: (1) the expense would be recoverable under Department precedent if it were incurred during a test year; (2) denying the deferral would significantly harm the company's overall financial condition; and (3) denying the deferral is likely to cause the filing of a rate case that includes in the test year the expense for which deferral is sought. NSTAR has not met any of these three elements of the *prima facie* test. Neither the booked expense amount nor the Additional Minimum Liability are recoverable under Department precedent. *Fitchburg Gas and Electric Light Company*, D.T.E. 02-24 / 02-25, pp. 111, 115 (2002) ("[t]he Department's general policy with respect to pension expense is to limit rate recovery to test year cash contributions to the pension plan because accrual-based pension cost estimates generally cannot be shown to be annually or periodically recurring.") ("[t]he Department has found that the actual cash contribution to a tax-deductible trust strikes a balance of interests between shareholders and ratepayers ....") The Company has not demonstrated with any facts that, even with a write-off of equity, its bond ratings actually will be reduced or that any such reduction would significantly harm NSTAR's strong overall financial condition or harm ratepayers more than the additional costs associated with the requested deferrals.<sup>2</sup> Finally, denying the deferral will not cause a rate case; the Company told the Attorney General that it intended to file rate cases in 2003 months before this issue even arose.

Once a *prima facie* showing is made, the Department will evaluate the petition, considering such additional factors as: (a) the company's ability to choose a test year; (b) the company's history and frequency of rate increases; (c) the company's frequency of requests for deferrals; (d) the company's earnings in the year the subject expense was incurred; and (e) whether some voluntary agreement on the part of the petitioner (e.g., a settlement) would otherwise preclude bringing a rate case during the period for which deferral is sought. Granting a deferral does not guarantee recovery of the subject expense in a future rate case. Rather, subsequent ratemaking treatment of the expense would be considered in the company's next rate case. Regarding these additional factors, the Company may elect to file a rate case as early as March of 2003 for effect after the expiration of the four year merger "rate freeze" period.

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<sup>1</sup> The Department's policy behind granting deferrals is based in administrative efficiency: to avoid unnecessary rate cases which would be triggered by certain extraordinary pretest year expenses.

<sup>2</sup> To the contrary, NSTAR's strong "A" bond ratings have not dropped even after the Company announced in November, 2002, the expected effects on its balance sheet of the pension and PBOP accounting.

NSTAR reported earnings of 12.1 percent for 2001, and the consensus forecast for 2002 is for similar strong earnings.

The Company's request also raises questions under the Department ordered "rate freeze" associated with the NSTAR merger. *BEC Energy / ComEnergy*, D.T.E. 99-19, pp. 5, 25, 85 (1999).<sup>3</sup> According to Department precedent, a utility may not defer a cost during the period covered by a rate settlement that fixes rates unless specifically allowed by the terms of the agreement. *North Attleboro Gas*, D.P.U. 93-229, p. 6 (1993) (denial of deferral request since expense occurred during period of settlement and expense did not qualify as an exogenous cost). Through the settlement, a company's election to limit its rates for a number of years also "forecloses its ability to file for and therefore recover rates beyond those specified" in the agreement. *Id.* It now appears that NSTAR seeks ongoing accounting deferrals for periods covered by the freeze and beyond.

Therefore, NSTAR has failed to establish a *prima facie* case. The Department should either deny the petition outright or at least hold a hearing on the Company's proposal for the following reasons:

- (1) The Company has not established that the "true-up" amount is an extraordinary operating expense that Department precedent would allow as proper for deferral, *Boston Gas Company*, D.P.U. 89-177, pp. 7-8 (1989), or that the costs are recoverable from customers in a subsequent rate case.
- (2) The Company has not established the level of pension and PBOP expenses in the Company's rates. The relevant rates of the distribution companies were fixed by settlement or rate cases that are as much as ten years old.<sup>4</sup> Several of the NSTAR companies rates were set in settlements; in the settled rate cases there are no Department findings on the specific dollar amounts of individual costs, including pension and PBOPs.
- (3) The Company has not established that the pension and PBOP expenses cannot be changed from year to year simply by making minor changes in actuarial assumptions, thus directly affecting the regulatory asset balance.
- (4) The Company has not established that any of the individual distribution companies will

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<sup>3</sup> The Attorney General has appealed the merger decisions in *BEC Energy / ComEnergy*, D.T.E. 99-19 (1999) and frames his arguments, as he must, in this case with the understanding that the Department's order is in effect until modified or overturned by the Massachusetts Supreme Judicial Court. As the appeal is still pending, nothing in these comments should be construed as an adverse admission or waiver of any legal or factual argument that the Attorney General has made in the pending appeal.

<sup>4</sup> The Company's kilowatt-hour sales have increased by 19 percent in the last ten years; revenues being collected through rates are therefore higher than the amounts found in those cases.

experience severe detrimental financial effects without the proposed deferral. In fact, NSTAR reported to the financial community an estimated \$200 – \$300 million impact of this accounting at end of the third quarter, yet the Company's bond rating has not changed, and the evidence does not show that the Company is having difficulty attracting capital. This transaction is not a cash outlay, rather it is an accounting accrual apparently recorded by the holding company.

- (5) The Company has not established the actual amount of the deferral and references stale data. The Company accounted for its pension and PBOPs trust fund assets for the most recently reported quarter, September 30, 2002. Since that time the stock market has risen 18 percent. The Company has failed to indicate what the expected deferral amount will be by December 31, 2002.
- (6) The Company indicated that this accounting problem is for the year 2002 and the situation will reverse in 2003. The Company, however, has not indicated what the Department should do if the situation reverses itself in 2003.

While the Attorney General is concerned about NSTAR's allegations that denial of the petition could lead to detrimental financial consequences that may harm customers, the Company has not shown that such consequences will in fact result notwithstanding NSTAR's strong financial position overall. The Company has made a number of statements that require further examination, discovery and briefing. Since NSTAR failed to provide a sufficient factual basis to support its proposed calculations and the requested deferral, the Department should either deny the petition outright or at least allow discovery and conduct a hearing to fully examine the issues and determine the facts before ruling on the request.

Sincerely,

Joseph W. Rogers  
Division Chief  
Utilities Division

cc: Service list